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'87 Annual Reports Sport a Few New Features

By JOHN P. FORDE

NEW YORK

WHO reads these things, anyway?The question is a common one this time of year, as the annual reports start to roll in. And it is asked by just about everyone in a position to receive the annuals of major banking and industrial companies — equity and debt analysts, major investors, special interest groups, and financial journalists.

The 1987 annual reports of major regional and money center banking companies will reflect the demands of some very significant readers, primarily regulators and representatives of investors. They've made their voices heard and prevailed on companies to provide increased information on areas like income taxes, loan fees, and Third World debt.

As in prior years, the 1987 annual reports will be part regulatory disclosure, part financial explanation, part fashion show, and part high school yearbook. They can also be part apology and, some bankers say, part information too technical for the average reader to understand.

SOME bankers last year used this line of reasoning to criticize a Financial Accounting Standards Board proposal on disclosure of financial instruments. The bankers said the panel that sets accounting rules overstated the financial knowledge of the average annual report reader.

Subjects such as offsetting foreign exchange interest rate swaps and various types of off-balance-sheet liabilities may be too intricate for the average reader to comprehend, they claimed.

Consultants are devising ways to give the right amount of information to investors who need it. For example, a new type of annual report, called the summary annual, is being prepared by at least one regional banking company. The report is shorter and contains less financial information than standard annuals. It's being touted by its developer,

Annual: Page 6

Tom Bloom

Optima Causes Some Backlash Among Banks

Angry Institutions Drop American Express Line

By MICHAEL WEINSTEIN

Last of a Series

Some banks have stopped marketing American Express products since the company unveiled its Optima credit card, according to the *American Banker's* second annual credit card survey.

Eight out of 60 financial institutions said they have stopped offering American Express travelers checks or American Express gold cards since the announcement of Optima, a card that offers a revolving line of credit and that is similar to the MasterCard and Visa bank cards.

Top Premium Card Issuers
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The traditional green American Express card is a charge card, so cardholders must generally pay off outstanding balances by the end of each billing cycle.

Last June, the *American Banker* mailed about 110 questionnaires to the nation's biggest financial institutions and top credit card banks. Sixty responses were received by mail or by telephone in the following months.

The survey's results, while not statistically significant, highlight a trend some bankers said they have noticed among their peers. For its part, American Express said it has seen no bank flight from its products.

For years, banks and American Express have teamed up to deliver financial products to consumers and make money in the process.

Many banks sell American Express travelers checks, and the company

Banks Drop: Page 22

Today

The Tax Reform Act of 1986 is making it less profitable for U.S. banks to conduct business abroad. Accountants say the full effects may not be felt until banks submit 1988 returns. 2

Robert C. DiGennaro, the former president and chief executive officer of Suffield Savings Bank, has been indicted by federal grand juries on charges related to insider trading. He allegedly disclosed confidential information about the merger of the Suffield, Conn., thrift with Coastal Bancorp of Portland, Maine, before it was made public. 3

The Connecticut Banking Department has filed suit to force the First National Bank of Stamford to curtail its 18-month-old courier service used to pick up customers' deposits. 3

MNC Financial has shown that most experts were wrong when they predicted it would take many years to make up the earnings dilution caused by its merger with American Security Corp. 24

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COMMENT

A walk with Paul Volcker reveals a hard-nosed glimpse of the future, writes Dr. Paul S. Nadler. 4

NEWS MONDAY

Sen. Christopher Dodd won a good deal of what he sought in the Glass-Steagall repeal that emerged from the Senate Banking Committee. The package, which calls for banks to phase in securities activities and restricts their insurance powers, largely reflects that nobody on the committee wanted to vote in this election year. 3

The first lesson in lobbying is to always make an appointment with a lawmaker before you arrive, as a group of trust bankers learned on a recent tour of Capitol Hill. 15

A VIEW FROM OUTSIDE

MARTIN MAYER

Panama and the Banks

GEORGE D. MOFFETT 3d, who was assistant to the chief of staff in the Carter White House, describes the banking laws of Panama in his book, "The Limits of Victory," about the campaign to ratify the Panama Canal Treaties. "The legal environment," he writes, ". . . provided total freedom to carry on intermediary business in foreign currencies with no central bank regulations, no controls on the movement of capital, no bookkeeping requirements, no access to records for foreign authorities, no reserve or liquidity requirements, and, best of all, no taxes."

This total exemption from the slings and arrows of outrageous fortune was set up in 1969 by Nicholas Ardito Barletta, who was then planning minister and later the first of two presidents of Panama dismissed by Gen. Manuel Antonio Noriega. Mr. Barletta saw easy bank licensing and supervision as a source of income for Panamanians and, not least, for the government of Panama.

And, of course, as a source of loans. Mr. Moffett's book cites an unnamed "American banking official in Panama" who noted, among the benefits the host country derived from this arrangement, that "the banks lend freely to the government of Panama."

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BANKING TRENDS

A Walk in the Economic Woods with Volcker

By DR. PAUL S. NADLER

WALKING DOWN THE street with Paul Volcker makes you feel important. It reminds me of the time someone was said to have asked J.P. Morgan for a loan, to which he replied: "I won't lend you money, but for a fee, I'll walk down Wall Street with my arm around you."

Mr. Volcker and I were in Orlando speaking at a users conference sponsored by the Kirchman Corp., the Florida software company. Walking with him afterward, I felt more significant than at any time since I went to a men's room with Henry Kissinger, where we had a bodyguard at each corner while we were inside.

Everyone recognizes the 6 foot 9 inch former chairman of the Fed — many come up and ask to have a picture taken with him. Mr. Volcker is so charming and kind it is hard to remember that until recently he was the second most important person in America in the mind of this observer and many others.

Of course fame dies quickly. Another attendee at the Kirchman conference reportedly went up to Mr. Volcker and queried, "Didn't you used to be Paul Volcker?"

But talk to him, and his thinking continues to show the impact of his years as a central banker.

• He was asked whether the regulations weren't crazy that require a bank to raise more capital if it realizes bond losses and marks the portfolio to market, while a bank is considered adequately capitalized if it does not take this step of realizing losses. His reply: "Anything that can force banks to raise more capital is all to the good."

Nadler Says:

Volcker gave a message that needs repeating, again and again: We are living beyond our means and will have to pay for it through a lower standard of living sooner or later.

• He was asked whether unfriendly takeovers of banks are good or bad for the nation. His negative response is couched in terms of fear for the strength of the bank rather than any other consideration.

• He was told that an employee of Bankers Trust Co. quit when his bonus was only $3 million after he had made a fortune for the bank in the foreign exchange market. Mr. Volcker's response was that no bank should allow the type of exposure that could lead to such foreign exchange profits, because it could lead to equal-size losses and thereby seriously damage the bank.

• And he was asked about the possibility that Black Monday might force the Congress and the President to do something about the budget deficit. He responded that for three days it appeared these governmental groups were scared and "got religion." But after that, it was back to business as usual. He added during his question and answer period at the convention that we may have to see another Black Monday before we truly do the job on the deficit that needs to be done.

A Mexican Reflection

While it was fun to walk and talk with the former head of the Fed, it was in his remarks to the convention that he was truly marvelous. Mr. Volcker gave a message that needs repeating, again and again: We are living beyond our means and will have to pay for it through a lower standard of living sooner or later.

To this listener at his breakfast talk, the most interesting comment he made was to compare us with Mexico seven or so years back.

The Mexican financial officials went to their president and complained that the nation needed fiscal discipline. But at that time Mexico was able to borrow all the money it wanted from U.S. banks, so the president dismissed the financial aides and continued with business as usual.

Later, when those banks stopped lending new sums to Mexico, the nation's finances went to pieces, and the peso dropped from about 12½ to the dollar to about 2,500 to the dollar.

Similarly, while foreigners still will lend us enough to cover our budget deficits, no presidential candidate is willing to talk about the economy without pledging to be against any tax increases or spending cuts. In Mr. Volcker's opinion, we may well suffer the same economic decline as Mexico when our ability to borrow abroad halts.

Already we have seen a cutoff of private investment in the United States, so the basic financing of our deficits must now come from central banks and governments, Mr. Volcker said.

With interest cost on the debt rising steadily as the deficit continues to burgeon, with more older people in the nation pressuring for more entitlement spending, and with limits to military cutbacks, he continued, we are in for trouble, because we do not have the productive capacity to grow out of our debt problems.

What about productive capacity? The dollar has dropped enough, and U.S. labor costs are now competitive in world markets, being lower than those in Europe and equal to those in Japan.

(Go to Epcot Center, as this writer did before the meeting. See the robot at the General Motors Corp. exhibit that can do all the dirty work that formerly required high-cost manual labor, and you can verify the success of United States in cutting labor costs sharply in the recent past.)

So the outlook, according to Mr. Volcker, is likely to be a lower dollar, higher interest rates, recession here and abroad, and stagflation, unless we do something soon.

Consumption Tax to the Rescue

What should we do? Mr. Volcker said the solution must come largely on the revenue side. As indicated above, spending cannot be cut much further, but there are real possibilities in consumption taxes.

Sure, we must do something about entitlements, like taxing Social Security benefits, modifying eligibility, and reducing cost of living adjustments.

But to Mr. Volcker the most important way we can work on the deficit is to pass a gas tax increase that brings in $50 billion to $60 billion a year, to raise cigarette and liquor taxes, and otherwise tax consumption.

"Democracy always waits for crises to take necessary steps, but this time the risk is too great," he concluded.

Changing the income tax again is not in Mr. Volcker's proposed agenda, but some changes in government's role and revenue sources are necessary.

He said that we are likely to have a new energy crisis within a few years; therefore we must curb our deficits $30 billion to $40 billion a year to keep foreign owned funds willing to finance it. If nothing else works, he said, the market will force change eventually through another Black Monday, at great risk to the nation.

"We always felt that our economy would continue to grow and our children would always be richer than we are," he said. "This is no longer true unless we do something to build productivity and halt the policy of consumption that vastly exceeds production."

In sum, Mr. Volcker has a major warning for the future because of our unwillingness to face economic reality today, and his warning is not pleasant.

Walking with him and thinking of the responsibility of the Federal Reserve in such an environment, I had to feel that at times he is pretty happy that he has given up the mantle of Fed — and that people now come up and ask him, "Didn't you used to be Paul Volcker?" ■

Dr. Nadler is professor of finance at Rutgers University's Graduate School of Management and is contributing editor of the *American Banker*.

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Editor: William E. Zimmerman
News Editor: Thomas J. Ferris
Associate Editors: Laura Gross, Sanford Rose, David O. Tyson

NEWS BUREAUS:
Washington: Chief, Robert Trigaux, 911 National Press Building, Washington, DC 20045; (202) 347-5529
Midwest: Chief, Richard Ringer, 53 W. Jackson Blvd., Suite 230, Chicago, Ill 60604; (312) 663-6380
West Coast: Chief, Robert Luke, Suite 320, 510 W. Sixth St., Los Angeles, CA 90014; (213) 627-0953
San Francisco: Chief, Michael A. Robinson, 450 Sansome Street, Suite 1420, San Francisco, CA 94111; (415) 986-8705
Southwest: Chief, David LaGesse, Suite 1600, 8080 North Central Expressway, Dallas, TX 75206; (214) 891-8878
New England: Chief, Michael Weinstein, 210 South St., Boston, MA 02111; (617) 542-6848
London: Chief, John J. Duffy, American Banker, c/o Infopac S.A., 31-35 Beak St., London W1R 3LD England; (01) 439-3066

Feature Editions Editor: Patricia Stundza
Chief Statistician: L. Michael Cacace
Senior Editor, Copy Desk: Aileen L. Kyte
Art Director: Pamela Budz
Contributing Editor: Paul S. Nadler

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OVERVIEW

Why Do They Want to Be President?

By H. ERICH HEINEMANN

BY TOMORROW evening, the nation should finally get a clear picture of who the serious contenders will be for the White House in November. Voters in 20 states — mostly Southern, but also in the Northeast and West — will select roughly one-third of the delegates to the national party conventions this summer.

For practical purposes, the race should narrow to Vice President George Bush and Senate Minority Leader Robert Dole for the Republicans and Massachusetts Gov. Michael Dukakis and Missouri Rep. Richard Gephardt for the Democrats. While the contest won't be over by a long shot, the candidates now must start to shift their priorities to the painful issues that will confront the next administration, no matter who is elected.

The 1980s have brought radical changes to America. An enormous federal deficit (bigger than those of all previous administrations combined) has spawned a host of toxic side effects.

These include an unprecedented shortfall in international trade, the emergence of the U.S. as the world's largest debtor nation, the takeover of America by foreign investors, and, not least, the prospect of a significant curtailment of U.S. living standards in the 1990s. It makes you wonder why such a group of vigorous, otherwise intelligent men would even want to work at the White House, let alone be President.

Debt May Overshadow All

These developments will all pose major challenges to the next administration. Over the long run, they may pale in comparison with the fallout from the U.S. debt buildup and the concurrent erosion in credit quality. While the economy is growing, serious problems will be postponed.

However, a day of reckoning will come. The worst case would be a credit implosion — widespread, destructive defaults analogous to the collapse in the 1930s. While possible in theory, that outcome is very improbable. It is much more likely that the next President will have to present U.S. taxpayers with a humongous invoice for the cost of repairing the financial system.

A large part of the problem is the sheer size of the debt. Total nonfinancial debt (consumers, businesses, governments) was $3.6 trillion in 1980; it is $8.3 trillion today. More important, debt has grown much faster than the economy.

The debt-GNP ratio was about 1.3 to 1 at the beginning of the decade. It is now almost 1.8 to 1. Put differently, if the debt ratio today were the same as in 1980, total debt would almost $2.5 trillion lower than it actually is.

The party line at the White House is that these debt levels (and particularly the foreign debt) really don't matter much. As the President's Council of Economic Advisers put it in its annual report, "Even at $400 billion, net foreign claims on the United States are not large relative to the income that can be used to service them."

In an absolute sense, that statement is true at present. However, a dynamic process is under way. U.S. foreign debt is growing at a rate of more than $3 billion per week. In effect, the U.S. must go overseas to borrow the interest and dividends it owes its foreign creditors. Compound interest is a great concept if

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Banks Drop American Express After Optima's Introduction

Continued from Page 1

shares with banks the revenues generated by the sales. Traditionally, when a consumer signed up for an American Express gold card, a bank extended the line of credit that came with the card.

But in recent years, American Express has begun offering a wide array of financial products to consumers, and some bankers think an erstwhile teammate has become a threatening competitor. These bankers feel they are welcoming a Trojan horse into their branches by selling American Express products to their own customers.

American Express declined to say how many Optima cards have been issued.

When American Express announced its Optima credit card during March of last year, some bankers were outraged that the company would be competing directly with bank credit cards. Charles T. Russell, president of Visa U.S.A. Inc., sent a letter to the nation's bankers urging them to stop marketing American Express products.

Downplaying Travelers Checks

Since then, several banks have been downplaying American Express travelers checks, said Joel P. Friedman, director of strategic management at Arthur Andersen & Co. in San Francisco. "They might hide a stack of American Express travelers checks under the counter if someone comes in on their knees begging."

American Express is a venerable name in the travelers check business, but in recent years MasterCard and Visa have introduced their own travelers check products.

"I think Optima was the straw that broke the camel's back," said K. David Elgena, president of First City Bank-Sioux Falls NA in South Dakota, a credit card subsidiary of First City Bancorporation of Texas Inc., Houston.

Signet Bank, Richmond, Va., stopped selling American Express travelers checks in May 1987. "We felt that American Express was more of a direct competitor," said S. Joseph Ward, vice president at Signet.

Signet now sells MasterCard travelers checks in U.S. dollars and Thomas Cook checks, which are endorsed by MasterCard, in foreign currencies.

"We haven't seen any decline in the sale of travelers checks," Mr. Ward said.

Wells Fargo Bank stopped offering credit lines for American Express gold cards last spring, but Henry Silver, a vice president at the San Francisco bank, said that the company's move was coincidental with the Optima announcement.

Signet Bank, Richmond, Va., now sells MasterCard travelers checks in U.S. dollars and Thomas Cook checks, which are endorsed by MasterCard, in foreign currencies.

"It just wasn't a significant piece of our business," Mr. Silver said.

There is no apparent alarm at American Express.

"We've seen no negative impact as a result of Optima," said Tom Cash, senior vice president at American Express Travel Related Services Co.

He claimed that American Express has boosted its market share of the travelers check business in the last year. The company historically refuses to disclose specific market share data for travelers checks.

American Express travelers checks are sold at about 150,000 outlets, mainly branches of financial institutions.

"Gold card is going along extremely well," Mr. Cash added. American Express has seen no decline in bank participation in the program, which now includes about 2,300 banks.

Recently, American Express has begun using a Delaware bank subsidiary to extend credit to gold cardholders, but Mr. Cash said commercial banks remain an important part of the program. "We're anxious to increase participation by banks," he said. ■

Maryland Bank Leads in Premium Cards

Maryland Bank, Newark, Del., is the nation's biggest issuer of premium bank cards, according to the *American Banker's* second annual survey.

Maryland Bank has concentrated on attracting premium cardholders, and they represent about 31% of the bank's total credit card accounts.

Nationally, 4.6% of all Visa cardholders have premier Visa cards, according to Visa U.S.A. Inc., San Mateo, Calif.

Premium card accounts are generally more profitable for banks than standard credit cards because premium cardholders maintain higher balances.

Like Maryland Bank, other top premium card-issuing banks have an unusually high level of premium cards.

According to the newspaper's survey, premium card accounts represent 54% of total accounts at Colonial National Bank USA, Wilmington, Del., a subsidiary of TSO Financial Corp., Horsham, Pa.; 25% of total accounts at State Street Bank and Trust Co., Boston; and 10% of total accounts at NCNB, Greensboro, N.C.

Premium card accounts amount to about 5% of credit card accounts at Bank of America, according to the survey.

— Michael Weinstein

Top Premium Card Issuers

Of those responding to the American Banker survey

	Total accounts 12/31/86
1. Maryland Bank NA, Newark, Del.	562,800
2. Bank of America, San Francisco	288,000
3. Colonial National Bank USA, Wilmington, Del.	158,000
4. State Street Bank and Trust Co., Boston	140,000
5. NCNB, Greensboro, N.C.	88,200
6. Wells Fargo Bank, San Francisco	77,300
7. Signet Bank, Richmond, Va.	62,200
8. Equibank (Delaware) NA, Wilmington, Del.	45,500
9. MBank USA, Wilmington, Del.	44,200
10. Security Pacific National Bank, Los Angeles	40,000
11. BancOhio, Columbus, Ohio	37,000
12. Bank of New England, Boston	34,000
13. Dollar Dry Dock Savings Bank, White Plains, N.Y.	31,300
14. NBD Bancorp, Detroit	28,000
15. Indiana National Bank, Indianapolis	27,000
16. Citizens and Southern National Bank, Atlanta	25,000
17. Rocky Mountain BankCard System Inc., Denver	22,000
18. United Missouri Bank of Kansas City	22,000
19. United Virginia Bank, Richmond	20,000
20. Barnett Credit Services Inc., Jacksonville, Fla.	15,500
21. First Bank of South Dakota NA, Sioux Falls	13,300
22. First RepublicBank Dallas	12,900
23. AmSouth Bank NA, Birmingham, Ala.	12,400
24. Society National Bank, Cleveland	11,000
25. PNC National Bank, Wilmington, Del.	10,400
26. Connecticut National Bank, Hartford	10,000
27. First Maryland Bancorp, Millsboro, Del.	9,900
28. First Interstate Bancard Co., Simi Valley, Calif.	9,200
29. Meridian Bancorp, Reading, Pa.	9,200
30. Seattle First National Bank	8,600
31. Rainier Bank, Seattle,	6,900
32. California First Bank, San Diego	5,100
33. First Tennessee Bank, Memphis	5,000
34. Wachovia Bank & Trust Co., Winston-Salem, N.C.	5,000
35. Shawmut Bank, Boston	5,000
36. Bank of Hawaii, Honolulu	4,800
37. Sovran Bank/Delaware, Dover	4,500
38. Goldome FSB, Buffalo	4,500
39. First City Bank - Sioux Falls, S.D.	4,000
40. National City Bank, Cleveland	2,500
41. Fleet National Bank, Providence, R.I.	2,300
42. Empire of America, Buffalo	2,100
43. Sovran Bank NA, Richmond, Va.	2,000
44. Mellon Bank (Delaware), Wilmington	1,800
45. Midlantic National Bank/North, West Paterson, N.J.	1,500
46. European American Bank, Uniondale, N.Y.	1,200
47. South Carolina National Bank, Columbia	1,000
48. United Bank of Denver	1,000
49. Huntington National Bank, Columbus, Ohio	700
50. First Pennsylvania Bank NA, Philadelphia	500

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